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ONG KENG HUAT v. FORTUNE FRONTIER (M) SDN BHD & ANOR

HIGH COURT MALAYA, JOHOR BAHRU
MOHD NAZLAN GHAZALI JC
[ORIGINATING SUMMONS NO: 24NCVC-45-01-2015]
B 25 JUNE 2015

COMPANY LAW: *Members' rights – Derivative action – Leave of court – Trespass and unlawful occupation of company's land – Whether plaintiff as company director could initiate proceedings on behalf of company – Whether plaintiff acted in good*
C *faith – Whether plaintiff must be a minority shareholder to initiate action – Whether second defendant as company director assisted third party to commit trespass on company's land – Whether a valid tenancy agreement entered into between parties – Whether action could be brought against third party – Conduct of second defendant – Whether resulted in breach of duty for conflict of interest –*
D *Whether it was in best interest of company for leave to be granted – Companies Act 1965, ss. 181A & 181B*

The plaintiff filed an application for leave under s. 181A of the Companies Act 1965 ('the Act') to bring a statutory derivative action on behalf of the first defendant company against parties he deemed responsible for the
E trespass and unlawful occupation of the first defendant's land. The plaintiff and the second defendant equally owned shares and were the only directors of the first defendant. Disputes arose when the second defendant's son ('TWR'), who was the owner of a landed property adjacent to the first defendant's landed property, rented the first defendant's land to China State
F Construction since the latter needed a larger space to house its workers and store machineries. TWR and China State Construction entered into a tenancy agreement in respect of TWR's land and the first defendant's land, the latter by way of a sub-tenancy in TWR's capacity as its purported tenant. However, the plaintiff alleged, *inter alia*, that (i) no valid tenancy agreement
G was entered into in relation to the first defendant's land; (ii) the first defendant's land was rented at a lower rate compared to TWR's land; (iii) China State Construction paid the rental to TWR and the first defendant did not receive the rental payments; (iv) there was a failure to convene a board of directors' meeting; (v) the second defendant refused to cooperate
H with and assist the plaintiff to protect the first defendant from suffering losses due to China State Construction and TWR's actions; and (vi) there was no resolution issued by the board of directors of the first defendant authorising the first defendant or any other representative to deal with China State Construction and TWR in respect of the first defendant's land. The issues that arose for consideration were (a) whether the plaintiff was a complainant
I under s. 181A of the Act; (b) whether the plaintiff acted in good faith under

s. 181B(4)(a) of the Act; (c) whether it was in the best interest of the company as per s. 181B(4)(b) of the Act for leave to be granted; (d) whether the plaintiff must be a minority shareholder to initiate an action under s. 181A; (e) whether the insider wrongdoer benefited from the default in a s. 181A action; and (f) whether s. 181A of the Act could be invoked to permit a plaintiff, on behalf of the company in a derivative action, to commence action against a third party wrongdoer against whom the company may have a cause of action related to the alleged wrongdoing. The second defendant, however, argued that the plaintiff had been involved in the negotiations and had orally agreed with the material terms of the tenancy agreement prepared by the plaintiff's solicitors in relation to the first defendant's land. As such, the second defendant counterclaimed for a declaration that there was a valid tenancy agreement between the first defendant and TWR.

Held (allowing plaintiff's application; dismissing second defendant's counterclaim):

(1) A derivative action is instituted by a member of a company premised on a cause of action which belonged to the company. The provisions on statutory derivative action embodied in ss. 181A to 181E of the Act are designed to make it possible for a shareholder to overcome the limitations of the common law derivative actions. Section 181A, however, expressly provides that the right to bring common law derivative action is not abrogated (*Abdul Rahim Aki v. Krubong Industrial Park (Melaka) Sdn Bhd & Ors*; refd). (paras 27 & 28)

(2) The plaintiff was a director of the first defendant and had fulfilled the requirement under s. 181A(4)(c) of the Act which refers to "any director of the company". The *raison d'etre* of statutory derivative action was the empowerment of shareholding related interest, permitting a minority shareholder to institute an action on behalf of the company. (para 32)

(3) The plaintiff had established good faith in accordance with s. 181B(4)(a) of the Act. The plaintiff honestly believed that a good cause of action existed and had a reasonable prospect of success. Further, the intended suit was not instituted for a collateral purpose. Whilst the primary private motivation of the plaintiff was to seek a higher rental for the land, that in itself was neither surprising nor improper given his status as a 50% shareholder of the first defendant. The plaintiff had been consistent in insisting for high rentals. The plaintiff had a reasonable prospect of his claim on behalf of the first defendant being successful. Further, the plaintiff showed that instituting the derivative action was *prima facie* in the best interest of the first defendant. (paras 50, 51, 59, 61 & 65)

(4) The second defendant's action and conduct of being supportive to TWR were not by themselves necessarily improper but constituted a dereliction in his fiduciary duty since, *inter alia*, (i) the tenancy directly involved the interest of the first defendant; and (ii) the second defendant did not cooperate with the plaintiff to have a formal board of directors' meeting or an EGM convened as requested by the plaintiff. The second defendant did not appear to demonstrate a conduct consistent with that expected of a responsible director and fiduciary of a company when faced with the situation. As a director, the second defendant stood in a dual relation which prevents unprejudiced exercise of judgment. (paras 55, 57, 58, 65 & 83)

(5) It is strictly not necessary for a plaintiff to be a minority shareholder in order to institute s. 181A of the Act. Even without the allegation of the defaulting director benefiting from the breach, a mere breach of duty of care by the director that caused loss to the company was sufficiently actionable under s. 181A. Further, it was not necessarily the case that an action under s. 181A could only be taken if the insider benefited from the wrong done to the company. The overriding focus of s. 181A should be on pursuing a derivative action against those who had wronged the company, who often were also but not necessarily the insiders who were preventing an action from being taken in the first place. However, instances where third parties may be involved and participated in the wrongdoing in collusion with insiders could not be discounted. (paras 71, 72 & 74)

(6) It is not a legal requirement under s. 181A of the Act that the insider in default must be a party to be sued by the plaintiff on behalf of the company. The crux of a derivative action is to allow a complainant to seek leave for the company to institute a suit for a cause of action which has a reasonable prospect of success which otherwise could not be pursued due to the involvement of a wrongdoer insider having the ability to prevent the filing of the suit by the company. (paras 73 & 74)

(7) An action against third parties could be legally justified in principle if the cause of action against third party arose from a breach by an insider or controlling element. Since derivative actions are for situations where the controller wrongdoer prevents actions from being taken, derivative actions would not be appropriate where (i) there were no such constraints; and (ii) the company decided not to pursue against a third party wrongdoer if such decision was not in any way influenced by the third party. There ought to be some form of collusion or acting in concert between the insider wrongdoer and the said third party to invoke an action under s. 181A against the latter. A derivative action under s. 181A may be instituted even against a third party wrongdoer if the wrong arose from the default of an insider. (paras 77 & 80)

(8) The trespass by TWR and China State Construction was made possible by the breach of fiduciary duty, or at least of a duty of care, on the part of the second defendant. As such, in addition to the fulfilment of the requirements for leave under ss. 181A and 181B of the Act, the derivative action by the plaintiff, who was technically not a minority shareholder, on behalf of the first defendant, may be commenced against TWR and China State Construction. Both were third parties who allegedly committed trespass against the first defendant given the offending role of the insider second defendant. The plaintiff was granted leave under s. 181A since he had satisfied the requirements of s. 181B(4), to commence an action on behalf of the first defendant against TWR and China State Construction. (paras 81 & 82)

Case(s) referred to:

Abdul Rahim Aki v. Krubong Industrial Park (Melaka) Sdn Bhd & Ors [1995] 4 CLJ 551 CA ***(refd)***

Ang Thiam Swee v. Low Hian Chor [2013] 2 SLR 340 ***(refd)***

Celcom (Malaysia) Bhd v. Mohd Shuaib Ishak [2010] 7 CLJ 808 CA ***(refd)***

Dato' Suhaimi Ibrahim & Ors v. Hi-Summit Construction Sdn Bhd & Anor; Konsortium Lapangan Terjaya Sdn Bhd & Ors (Interveners) [2013] 1 LNS 203 HC ***(refd)***

Foss v. Harbottle [1843] 67 All ER 189 ***(refd)***

Hengwell Development Pte Ltd v. Thing Chiang Chin [2002] 4 SLR 902 ***(refd)***

Iesini & Others v. Westrip Holdings Ltd & Others [2009] EWHC 2526 ***(refd)***

Lembaga Tabung Angkatan Tentera v. Prime Utilities Bhd [2012] 2 AMCR 521 ***(refd)***

Ontario Ltd v. Bernstein [2000] OTC Lexis 3480 ***(refd)***

Pang Yong Hock & Anor v. PKS Contracts Services Pte Ltd [2004] SGCA 18 ***(refd)***

Pavlides v. Jensen [1956] Ch 565 ***(refd)***

Primex Investments Ltd v. Northwest Sports Enterprise Ltd [1995] Can LII 717 (BCSC) ***(refd)***

S Vigneswaran M Sanasee v. Maju Institute of Educational Development (MIED) (No 2) [2011] 2 CLJ 678 HC ***(refd)***

Swansson v. RA Pratt Properties Pty Ltd & Anor [2002] NSWSC 583 ***(refd)***

Teh Swee Lip v. Jademall Holdings Sdn Bhd [2014] 8 CLJ 451 CA ***(refd)***

United Copper Securities So Et Al v. Amalgamated Copper Co Et Al [1917] 244 US 261 ***(refd)***

Wong Kai Wah v. Wong Kai Yuan & Anor [2014] SGHC 147 ***(refd)***

Legislation referred to:

Companies Act 1965, ss. 128, 131B(1), 181A(4)(c), 181B(4)(a), 181C, 181D, 181E
Contracts Act 1950, s. 2
Malaysian Code on Take-Overs And Mergers 1998, s. 20(1)

Business Corporations Act [Canada], s. 239
Companies Act (Chap 50) [Sing], ss. 216A(3)(b), (c), 216B
Companies Act 2006 [UK], s. 261(3)
Corporations Act 2001 [Aus], ss. 236, 237

Other source(s) referred to:

Halsbury's Laws of England, 4th edn, vol 45, p 6312

For the plaintiff - Sofian Shamsudin (NG Vinod & Rifhan Ili Roslan with him); M/s Tam Cheng Yau & Co
For the 2nd defendant - LM Looi (Wee Lee & Izatty Maria with him); M/s Dennis Nik & Wong

Reported by Kumitha Abd Majid

JUDGMENT

Mohd Nazlan Ghazali JC:

Introduction

[1] This case concerns an application by the plaintiff by way of an originating summons dated 21 January 2015, for leave under s. 181A of the Companies Act 1965, to bring a statutory derivative action on behalf of Fortune Frontier (M) Sdn Bhd, being the first defendant company, against China State Construction Engineering (M) Sdn Bhd ("China State Construction") and one Tan Wei Rong.

[2] I heard the application on 28 May 2015 and gave my decision to grant leave on 25 June 2015. This is my judgment, setting out the full reasons for my decision on the application which involves a number of important points on the scope of ss. 181A and 181B of the Companies Act 1965.

Salient Background Facts

[3] The plaintiff and the second defendant equally own the locally incorporated first defendant company, by virtue of the single share held by each, both of whom are also the only directors on the board of the first defendant company, with a paid up capital of RM2.

[4] Tan Wei Rong, the son of Tan Boon Leong, the second defendant, is the owner of a landed property under Geran Mukim 967, Lot 1737 Mukim Pulai, District of Johor Bahru ("TWR land"), which location is adjacent to a landed property owned by the first defendant, held under HSM 181, Lot 1363, Mukim Pulai, District of Johor Bahru ("first defendant's land").

[5] Tan Wei Rong had been negotiating with China State Construction to rent out TWR land. Given that access to TWR land is through the first defendant's land, and since China State Construction required larger space to house their workers, set up operations site office and store machineries, Tan Wei Rong suggested that the first defendant's land be rented to China State Construction as well.

[6] The plaintiff and the second defendant, being directors of the first defendant, agreed with the suggestion, provided the interest of the first defendant be safeguarded in any such transaction. The directors then agreed that Tan Wei Rong instruct Messrs Dennis Nik & Wong to draft a tenancy agreement for the purpose.

[7] Dissatisfied with the draft by Messrs Dennis Nik & Wong, the plaintiff instructed Messrs Woon Wee Yuen & Partners to prepare a new draft tenancy agreement.

[8] On 17 September 2014, Tan Wei Rong entered into a tenancy agreement with China State Construction in respect of both TWR land and the first defendant's land, the latter by way of a sub-tenancy in Tan Wei Rong's capacity as its purported tenant, notwithstanding the absence of a written tenancy agreement between the first defendant and Tan Wei Rong.

Grounds For Leave Application

[9] The grounds for the application are stated to be as follows:

(i) China State Construction and Tan Wei Rong had trespassed into the first defendant's land, causing losses to the first defendant. It is of relevance to mention that Tan Wei Rong is not a present or past member of the board of the first defendant;

(ii) the second defendant, despite being a director and 50% shareholder of the first defendant, had refused to cooperate with and assist the plaintiff to protect the first defendant and prevent the first defendant from incurring losses as a consequence of the actions and conduct of China State Construction and Tan Wei Rong;

(iii) the second defendant had failed in his duty as a director of the first defendant by putting personal interest before the interest of the first defendant, by way of in effect, preventing the first defendant from pursuing legal action against China State Construction and Tan Wei Rong, who is the second defendant's own son;

(iv) no income or profits had thus far accrued to the first defendant from the exploitation and unlawful occupation of the first defendant's land by China State Construction and Tan Wei Rong;

(v) there was no resolution of the board of directors of the first defendant authorising the first defendant or any other representative to deal with China State Construction and Tan Wei Rong in respect of the first defendant's land on behalf of the first defendant; and

(vi) plaintiff has therefore been prevented from initiating legal proceedings in the name of the first defendant.

[10] The second defendant counterclaimed against the plaintiff, mainly in seeking a declaration that there is a valid tenancy agreement between the first defendant and Tan Wei Rong in respect of the first defendant's land.

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The Plaintiff's Contentions

[11] The plaintiff contended that the terms contained in the draft tenancy agreement prepared by the law firm appointed by the plaintiff, Messrs Woon Wee Yuen were not agreed to by the second defendant and Tan Wei Rong, and whilst negotiations on the terms of the intended tenancy between the first
B defendant and Tan Wei Rong in respect of the first defendant's land were in progress, and despite the plaintiff not having given his agreement on the same, Tan Wei Rong had executed the tenancy agreement with China State Construction on 17 September 2014, giving access of the first defendant's land to the latter.

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[12] The plaintiff argued that the second defendant and his son, Tan Wei Rong had colluded to benefit themselves at the expense of the interest of the first defendant, whereby the first defendant's land had been agreed by Tan Wei Rong to be rented at a lower rate than in respect of TWR land to the same tenant. Further, it was alleged that China State Construction is
D presently paying rental to Tan Wei Rong, whilst the first defendant has not been receiving any rental payments.

[13] The plaintiff contended that given the inaction of the second defendant, he had instructed the company secretary of the first defendant to
E convene a board of directors' meeting of the first defendant. There was no response from the company secretary. Neither was there any reply when the plaintiff's solicitors, Messrs Tam Cheng Yau & Co wrote in their letter of 11 November 2014 to the company secretary to issue notice for an extraordinary general meeting of the first defendant be convened to discuss the alleged trespass and unlawful occupation by China State Construction on
F the first defendant's land.

[14] The plaintiff's solicitors' letter to China State Construction dated 10 November 2014 on the alleged trespass by the latter on the first defendant's land also went unanswered.

G **[15]** The plaintiff did receive a letter dated 15 November 2014 from Messrs Dennis Nik & Wong, solicitors for the second defendant (in reply to the plaintiff's letter of 10 November 2014) alleging that the plaintiff had agreed to the renting of the first defendant's land and that the transaction had been pursued with the agreement of the plaintiff. The plaintiff, through his
H lawyers responded in their letter of 18 November 2014, denying the allegations by the second defendant, refusing to retract his earlier letter of 10 November 2014 and giving notice that leave application under s. 181A of the Companies Act 1965 would be filed.

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[16] The plaintiff accordingly sought leave be granted by this court to enable the first defendant initiate proceedings against parties he deemed responsible for the trespass and the unlawful occupation and use of the first defendant's land, namely Tan Wei Rong and China State Construction, following the refusal of the second defendant, being the only other director of the first defendant to cooperate, thus at the same time allegedly participated in the wrong perpetuated against the first defendant.

The Second Defendant's Contentions

[17] The second defendant contended that the first defendant had, since the purchase of the first defendant's land on 10 January 1995 been trying without success to rent out the first defendant's land, even at low monthly rentals of between RM2,000 and RM5,000. A subsequent rental to a fish pond business also proved unsuccessful.

[18] That on 7 May 2014, two business middlemen approached the second defendant, proposing that the first defendant rent the first defendant's land to China State Construction at RM26,000 monthly on condition that RM12,000 out of the monthly rental be paid to the middlemen as commissions.

[19] The proposal was informed to the plaintiff and to facilitate negotiations, the plaintiff agreed with the suggestion to consider renting the first defendant's land to Tan Wei Rong and thus allegedly authorised Tan Wei Rong to negotiate with China State Construction because Tan Wei Rong was then already seeking to let his own TWR land, being adjacent to the first defendant's land, to China State Construction.

[20] The second defendant further contended that during the months of July and August 2014, discussions on the draft tenancy agreement took place involving the plaintiff, and even though Messrs Dennis Nik & Wong prepared the first draft, the second defendant agreed with the plaintiff's request for Messrs Woon Wee Yuen & Partners to act for the first defendant and prepare a new draft tenancy agreement instead.

[21] The parties then agreed that the tenancy agreement between the first defendant and Tan Wei Rong for the first defendant's land would be finalised by Messrs Woon Wee Yuen. In October 2014, Messrs Woon Wee Yuen enclosed a draft containing the agreed principal terms, and Tan Wei Rong suggested a number of comments which were not objected to by the second defendant.

[22] The second defendant thus contended that the plaintiff, having been involved in the negotiations, had knowledge of the same and had orally agreed with the material terms of the tenancy agreement prepared by the plaintiff's own solicitors, in respect of the first defendant's land and that execution of the same would therefore be a mere formality.

[23] That the crux of the plaintiff's dissatisfaction is the rental amount of payment from China State Construction, specifically on the distribution of the same as between the first defendant and Tan Wei Rong in respect of their respective lands. The plaintiff contended the rental for the first defendant's land was inequitable and in any event lower than that agreed with China State Construction for TWR land. The second defendant refuted this, claiming that the rental for the first defendant land was higher than for the TWR land and that in fact the former was even higher than what it ought to have been if the total per square feet of the respective lands was taken into account.

[24] The tenancy agreement dated 17 September 2014 between Tan Wei Rong and China State Construction had been made aware to the plaintiff. Yet the plaintiff issued a trespass notice to China State Construction on 10 November 2014 even though the principal terms between the first defendant and Tan Wei Rong had been finalised.

[25] The second defendant contended that the plaintiff's initial denial of knowing one of the middlemen (subsequently, effectively retracted and clarified after the filing of a statutory declaration by one of the said middlemen) as well as the plaintiff's subsequent stance, after the issuance of the trespass notice to China State Construction, that the plaintiff would only be agreeable to rent the first defendant's land for a much higher rental as stated in a handwritten note furnished by the plaintiff's son, showed that the plaintiff was not acting in good faith, especially when the draft tenancy agreement had been drafted on plaintiff's own instructions.

[26] The negotiations involving the plaintiff even agreed with the plaintiff's decision to not proceed with the earlier suggestion for the first defendant to grant a power of attorney to China State Construction.

The Law On Derivative Action

[27] The well established common law "proper plaintiff" rule in the case of *Foss v. Harbottle* [1843] 67 All ER 189 ("*Foss v. Harbottle*") provides that the courts will not interfere in matters concerning the internal management of a company and it is for the majority members to decide on the conduct of the affairs of the company. Thus, if a company suffers a wrong, *prima facie* it is the company itself that should institute an action to remedy the wrong done to it, and not any of its shareholders, as the company is a separate legal entity from its members. In the Malaysian case of *Abdul Rahim Aki v. Krubong Industrial Park (Melaka) Sdn Bhd & Ors* [1995] 4 CLJ 551, the Court of Appeal clarifies further the application of the rule in *Foss v. Harbottle* and the limited common law exceptions to the same developed over the years, allowing minority shareholders to institute proceedings, such as in respect of *ultra vires* act which cannot in any event be confirmed by the majority and where there is fraud on the minority by the wrongdoer in control. These two

and other exceptions are forms of derivative actions. A derivative action is thus one instituted by a member of a company premised on a cause of action belonging to the company instead of that of the member.

[28] The provisions on statutory derivative action embodied in ss. 181A to 181E of the Companies Act 1965, having come into force on 15 August 2007, are designed to make it possible for a shareholder to overcome the limitations of the common law derivative actions. Section 181A however expressly provides that the right to bring a common law derivative action is not abrogated.

[29] Given their importance to this application for leave by the plaintiff, the entirety of ss. 181A and 181B are set out hereunder:

Section 181A. Proceedings on behalf of a company

(1) A complainant may, with the leave of the Court, bring, intervene in or defend an action on behalf of the company.

(2) Proceedings brought under this section shall be brought in the company's name.

(3) The right of any person to bring, intervene in, defend of discontinue any proceedings on behalf of a company at common law is not abrogated.

(4) For the purposes of this section and sections 181B and 181E, "complainant" means:-

(a) A member of a company, or a person who is entitled to be registered as member of a company;

(b) A former member of a company if the application relates to circumstances in which the member ceased to be a member;

(c) Any director of a company; or

(d) The Registrar, in case of a declared company Under Part IX.

Section 181B. Leave of Court

(1) An application for leave of the Court under section 181A shall be made by originating summons and no appearance need to be entered.

(2) The complainant shall give thirty days notice in writing to the directors of his intention to apply for the leave of Court under section 181A.

(3) Where leave has been granted pursuant to an application under section 181A, the complainant shall initiate proceedings in Court within thirty days from the grant of leave.

A (4) In deciding whether or not leave shall be granted the Court shall take into account whether:

(a) The complainant is acting in good faith; and

(b) It appears *prima facie* to be in the best interest of the company that the application for leave be granted.

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[30] The leading case in Malaysia on the interpretation and application of ss. 181A and 181B is the decision of the Court of Appeal in *Celcom (Malaysia) Bhd v. Mohd Shuaib Ishak* [2010] 7 CLJ 808 ("*Celcom*"). In overturning the decision of the High Court which had granted leave to the complainant, the judgment of the Court of Appeal set a higher threshold for the statutory derivative action in this country. Abdull Hamid Embong JCA (as His Lordship then was) in his judgment for the Court of Appeal explained as follows:

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> The intention of ss. 181A to E of the CA is to enable a member, present or past, to seek leave to bring an action in the name of the company to recover losses sustained by that company. As such, leave to bring a derivative action must not be given lightly (see *Swansson v. RA Pratt Properties Pty Ltd & Anor* [2002] NSWSC 583). Thus, once leave is granted the defendants in this case cannot revisit the issue on the grant of leave. Granting leave is therefore final in that sense and not interlocutory in character. In this respect, the learned judge was wrong in stating cursorily that the matter before him was "only an application for leave" and relying on the low threshold used under O. 53 RHC (application for judicial review) ie, to determine if an application for judicial review is not frivolous or vexatious by relying on cases like *Clear Water Sanctuary Golf Management Bhd v. Ketua Pengarah Perhubungan Perusahaan & Anor* [2007] 6 MLJ 446. The learned judge must as a matter of judicial prudence exercise a greater caution in satisfying himself that the requirements under Section 181A of the CA are met. A low threshold of merely determining if there existed a *prima facie* case is therefore a wrong basis for granting the leave. There needs to be a strict interpretation of Section 181A of the CA, and compliance to those statutory requirements. (see *Charlton v. Baber* 21 ACIC 1671).

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[31] I shall now examine the provisions of ss. 181A and 181B and determine whether the case for leave has been properly established.

Analysis Of Facts And Application Of The Law

Question 1: Is The Plaintiff A "Complainant" Under S. 181A?

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[32] The first question to be determined is whether the plaintiff falls within the concept of a "complainant" who seeks leave to bring an action on behalf of and in the name of the company, as described under s. 181A(4) of the Act. The plaintiff submitted that as a director of the first defendant company, he fulfils the requirement of s. 181A(4)(c) which refers to "any director of a company". I find this acceptable but consider it even more compelling if

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the plaintiff had also contended that he also meets the criterion under s. 181A(4)(a) which refers to "a member of a company" since the plaintiff is a 50% registered shareholder of the first defendant, and taking into account the whole *raison d'etre* of statutory derivative action which is the empowerment of shareholding-related interest, permitting a minority shareholder to institute action on behalf of the company.

Question 2: Is The Plaintiff Acting In Good Faith Under S. 181B(4)(a)?

[33] The essence of the concept of good faith has been explained in *Celcom*. The relevant passage reads as follow:

> The second crucial requirement for the determination of the Court in granting leave is the need for the Respondent to show that he was acting in good faith in making this application. (Section 181B (4)(a)). The onus of proof here is on the Respondent on a balance of probabilities. The test of good faith is two-fold. One is an honest belief on the part of the Respondent, and two, that this application is not brought up for a collateral purpose.

[34] In stating the above test, the Court of Appeal followed the formulation expressed by the Australian case of *Swansson v. RA Pratt Properties Pty Ltd & Anor* [2002] NSWSC 583. Abdull Hamid Embong JCA (as His Lordship then was) further stated as follows:

> This second requirement will depend on the factual circumstances which comes before the Court. This was stated by Palmer J in Swansson, with these words:
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> > Nevertheless, in my opinion, there are at least two interrelated factors to which the courts will always have regard in determining whether the good faith requirement of Section 237(2)(b) is satisfied. The first is whether the applicant honestly believes that a good cause of action exists and has a reasonable prospect of success. Clearly, whether the applicant honestly holds this belief would not simply be a matter of bald assertion: the applicant may be disbelieved if no reasonable person in the circumstances could hold that belief. The second factor is whether the applicant is seeking to bring the derivative suit for such a collateral purpose as would amount to an abuse of process.

[35] It is therefore clear that to establish good faith, the questions to be asked in the instant case are the following:

(i) whether the plaintiff honestly believes that a good cause of action exists and that it has a reasonable prospect of success; and

(ii) whether the plaintiff is seeking to bring the derivative suit for such a collateral purpose as would amount to an abuse of process.

I should also add an observation, since this is not mentioned in *Celcom*, that the Court of Appeal's reliance on Australian precedents is by reason of the similarities in the legislative provisions on derivative actions found in ss. 236 and 237 of the Corporations Act 2001 to the Malaysian provisions in ss. 181A and 181B. The relevant provisions are as follows:

> Australian Corporations Act
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> Section 237(2) The Court must grant the application if it is satisfied that:
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> (a) It is probable that the company will not itself bring the proceedings, or properly take responsibility for them, or for the steps in them;
>
> (b) The applicant is acting in good faith;
>
> (c) It is in the best interests of the company that the applicant be granted leave;
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> (d) If the applicant is applying for leave to bring proceedings - there is a serious question to be tried; and
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> (e) Either:
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> (i) At least 14 days before making the application, the applicant gave written notice to the company of the intention to apply for leave and of the reasons for applying; or
>
> (ii) It is appropriate to grant leave though subparagraph (i) is not satisfied.

[36] In *Celcom*, the plaintiff, as a former member of Celcom applied for leave to sue the directors of Celcom, the ultimate holding company of Celcom, namely Telekom Malaysia Bhd ("TM"), Telekom Enterprise Sdn Bhd ("TESB"), as well as the directors of both TM and TESB. The plaintiff sought to recover the alleged loss and damages for the breach of an agreement between Celcom and De Te Asia Gmbtt purportedly caused by the directors of Celcom by Celcom entering into an agreement with TM, resulting in the issuance of new Celcom shares, all without the approval of De Te Asia Gmbtt.

[37] The Court of Appeal found that the decision of a committee of independent directors of Celcom formed to decide on the transaction with TM had been an exercise of a prudent business judgment and a commercial decision of the directors, and that the plaintiff did not allege that the independent directors had conspired with TM. The Court of Appeal thus held that the proposed action by the plaintiff did not have any reasonable prospect of success.

[38] In addition, in Celcom, the plaintiff had commenced a personal action which was virtually identical to the derivative action and with exactly the same reliefs being sought. The Court of Appeal found that there was an

inconsistency in the conduct of the plaintiff since in the personal action the plaintiff was pursuing against Celcom for damages whilst at the same time in the derivative proceedings, the plaintiff was attempting to recover on behalf of Celcom. The Court of Appeal was of the view that the plaintiff's action was suspect and that he was merely advancing his own interest. It was thus held that the plaintiff was not acting in good faith and leave ought not to have been granted.

[39] The intended action by the plaintiff in *Celcom* was based on allegations of breach of duty by the board of directors. The Court of Appeal also arrived at their finding that there was no reasonable prospect of success in the proposed action since the claim by the plaintiff that he ought to have been able to benefit from a higher mandatory take over offer price of RM7 per Celcom share was found to be fallacious. This is in view of the fact that a mandatory take over offer price must be based on the highest price paid by the offeror during the preceding six-month period (s. 20(1) of the Malaysian Code on Take-Overs And Mergers 1998). The allegation of fraud and conspiracy on the part of the proposed defendants was therefore baseless and lacking in evidence, as the same was based on the incorrect premise that the offer price should have been RM7 per Celcom share.

[40] Applying the good faith test approved in *Celcom*, the High Court in *Lembaga Tabung Angkatan Tentera v. Prime Utilities Bhd* [2012] 2 AMCR 521 ("LTAT") granted leave to the complainant, LTAT, a minority shareholder in Prime Utilities Berhad as there was evidence that the directors of the latter had failed to diligently pursue the recovery of the monies the company invested in an asset management company, including by not having filed its proof of debt to the winding up of the said asset management company.

[41] Leave under ss. 181A and 181B was also granted by the High Court in *S Vigneswaran M Sanasee v. Maju Institute of Educational Development (MIED) (No 2)* [2011] 2 CLJ 678 ("MIED") but the High Court did not have the benefit of the judgment of the Court of Appeal in *Celcom*. It is nevertheless instructive to note that the High Court emphasised that good faith should be decided according to the facts of each case.

[42] In my view as the High Court in MIED followed the lower threshold test of the High Court in *Celcom*, the analysis on proof of good faith ought to be read in light of the Court of Appeal's judgment in *Celcom*. In any event, the test of good faith as developed in the jurisprudence of the Malaysian statutory derivative action is in part influenced by similarities found in ss. 216A and 216B of the Companies Act (Chapter 50) (Act 42 of 1967) (Singapore), enacted in 1993, which in turn are modeled upon Canadian legislation. Part 17 of the UK Companies Act 2006 and Part 2F. 1A of the Corporations Act 2001 (Cth) of Australia as mentioned above, also embody provisions on statutory derivative actions which are especially insightful although not in *pari materia* with ss. 181A and 181B.

[43] The pertinent provisions of s. 239 of the Canada Business Corporations Act (RSC 1985 C-44) and s. 216A of the Singapore Companies Act are set out hereunder:

Canada Business Corporation Act

239. (1) Subject to subsection (2), a complainant may apply to a court for leave to bring an action in the name and on behalf of a corporation or any of its subsidiaries, or intervene in an action to which any such body corporate is a party, for the purpose of prosecuting, defending or discontinuing the action on behalf of the body corporate.

(2) No action may be brought and no intervention in an action may be made under subsection (1) unless the court is satisfied that:

(a) The complainant has given notice to the directors of the corporation or its subsidiary of the complainant's intention to apply to the court under subsection (1) not less than fourteen days before bringing the application, or as otherwise ordered by the court, if the directors of the corporation or its subsidiary do not bring, diligently prosecute or defend or discontinue the action;

(b) the complainant is acting in good faith; and

(c) it appears to be in the interests of the corporation or its subsidiary that the action be brought, prosecuted, defended or discontinued.

Singapore Companies Act

216A - (1) In this Section and Sections 216B -

"company" means a company other than a company that is listed on the securities exchange in Singapore;

"complainant" means:

(a) any member of a company;

(b) the Minister, in the case of a declared company under Part IX; or

(c) any other person, who in the discretion of the Court, is a proper person to make an application under the section;

(2) Subject to subsection (3), a complainant may apply to the Court for leave to bring an action in the name and on behalf of the company or intervene in an action to which the company is a party for the purpose of prosecuting, defending or discontinuing the action on behalf of the company.

(3) No action may be brought and no intervention in an action may be made under subsection (2) unless the Court is satisfied that:

(a) the complainant has given 14 days' notice to the directors of the company of his intention to apply to the Court under subsection (2) if the directors of the company do not bring, diligently prosecute or defend or discontinue the action;

(b) the complainant is acting in good faith; and

(c) it appears to be *prima facie* in the interests of the company that the action be brought, prosecuted, defended or discontinued.

[44] A recent decision of the Court of Appeal in Singapore in *Ang Thiam Swee v. Low Hian Chor* [2013] 2 SLR 340 ("*Ang Thiam Swee*") has further elaborated the analysis on the concept of good faith in the context of the statutory derivative action.

[45] In *Ang Thiam Swee*, the appellant and the respondent each held 10% of the company's shares and another member held the rest of the shares. The shares held by the latter were subsequently transferred to the official assignee as the member was declared a bankrupt for misappropriating the company's funds. The respondent applied for leave to commence an action under s. 216A in the name of the company against the appellant for an alleged breach of director's duties on the part of the latter since investigative reports revealed that the appellant, as a co-signatory of the company's accounts, had also similarly misappropriated the company's funds. The issues before the court was whether the requirements in sub-s. (b) and (c) of s. 216A(3) were fulfilled to justify the granting of leave to the respondent to institute the statutory derivative action.

[46] The court ruled that the onus was on the applicant to establish good faith on his part and the court must assess the motivations of an applicant in order to determine whether he is acting in good faith. Good faith was stated to be less dependent on the motives which trigger the application, but more on the purpose of the proposed derivative action, which must have a clear nexus with the company's benefits or interests. The motivations of the applicant would only amount to a lack of good faith if they revealed that the applicant's judgment was influenced by purely personal considerations. The applicant must demonstrate that he is genuinely aggrieved and that his collateral purpose is sufficiently consistent with the objective of doing justice to the company.

[47] The Court of Appeal took into account the approaches of the courts in Canada and Australia and observed that first, the Canadian courts generally consider the applicant's honest belief in the merits of the proposed statutory derivative action as a strong indicator of good faith, and secondly, the Australian courts refer to two interrelated factors, specifically whether the applicant honestly believes that a good cause of action exists and has a reasonable prospect of success, and whether the applicant is seeking to institute the derivative suit for such a collateral purpose as would amount to an abuse of process.

[48] The Court of Appeal in *Ang Thiam Swee* held that essentially, the primary consideration in determining an applicant's good faith is whether the applicant honestly believes that a good cause of action exists. An applicant thus lacks good faith if his motives for commencing the statutory derivative action tantamount to a collateral purpose unrelated to doing justice to the company. The court appears to prefer the test on the existence of collateral purpose developed by Australian courts, as adopted earlier by the Court of Appeal in *Celcom* as well.

[49] Applying the above to the facts, the Court of Appeal in *Ang Thiam Swee* found that the respondent had failed to discharge his burden of establishing that he was acting in good faith in making the application. Instead, the respondent had been actuated by a number of private motives which amounted to a collateral personal purpose of seeking, *inter alia*, to secure sole control of the company such that the court was not convinced that the respondent had an honest belief in the merits of the application. The court observed that there was a significant amount of ill will between the two attributed to disputes over a number of several financial related issues. Additionally, the respondent was unhappy at discovering that some of the dividends due to him had not been paid out and that the appellant had on the other hand, received a higher amount as directors' fees. Instead of establishing good faith, the court noted that the respondent appeared to be motivated as much by spite as by the prospect of personal gain, and that in the absence of any clear coincidence between the company's interests and his apparent collateral personal purpose of securing sole control of the company, it would be a patent abuse of process to allow the respondent to use the company as a vehicle for his private objectives.

[50] Having considered the test of good faith applied in the various case law authorities mentioned above, I am of the view that based on affidavit evidence available before the court, the plaintiff has on balance of probabilities established good faith in accordance with s. 181B(4)(a). I find that the plaintiff honestly believes that a good cause of action exists and has a reasonable prospect of success. I do not find sufficient evidence that the intended suit is instituted for a collateral purpose.

[51] In arriving at this finding, I have found, among others, that whilst the primary private motivation of the plaintiff is to seek a higher rental for the land belonging to the first defendant, that in itself is neither surprising nor improper given his status as a 50% shareholder of the first defendant. The plaintiff has been consistent in insisting on high rentals. He did agree with the proposal to rent out the first defendant's land. But he was unrelenting in wanting to ensure the first defendant secure the right price. His conduct or inaction concerning the discussion on the draft tenancy agreement intended

to be entered into between the first defendant and Tan Wei Rong, his discomfort with the involvement of the middlemen who would get paid higher than the monthly rental, his handwritten note as to what he considered to be the rental acceptable to him, all go towards evidencing his motives which I do not consider to constitute a collateral purpose as would amount to an abuse of process. Further, the High Court in *MIED* referred to an observation by Justice Tysoe of the Supreme Court of British Columbia in *Primex Investments Ltd v. Northwest Sports Enterprise Ltd* [1995] Can LII 717 (BCSC) as follows:

> where there is an arguable case, the applicant cannot be said to be acting in bad faith because he wants the company to pursue what he genuinely considers to be a valid claim ... an applicant advancing self interest is not necessarily acting in bad faith.

The presence of a private interest in my view cannot necessarily negate good faith if the same coincides with that of the company, especially given the shareholding structure of the company, and equally importantly, whether an analysis of the entire circumstances of the case established other evidence to suggest otherwise. In my evaluation, the answer is in the negative.

[52] On the other hand, the evidence demonstrates that the plaintiff sought to get the first defendant to enforce its rights as the owner of the first defendant's land. He attempted to get the first defendant to have the correct forum properly deliberate on the disagreement concerning the sub-lease *via* his request to the company secretary to convene a board of directors meeting as well as an EGM, both of which went unheeded, despite the plaintiff having the statutory right to requisition on EGM under the Companies Act 1965 and I presume, to call for board meetings under the articles of association of the first defendant. This practically resulted in a deadlock situation in the company.

[53] I am not convinced that a valid agreement on the tenancy exists between the first defendant and Tan Wei Rong. The various drafts of tenancy agreement do not evidence any indication of endorsement by the plaintiff. If anything, the affidavit evidence show that the plaintiff had always had issues with the drafts which in my view is a strong reason in itself that should have rightfully led the other intending contracting party, namely Tan Wei Rong to secure a properly executed agreement with the first defendant before entering into the tenancy with China State Construction with the purported right as the tenant of the first defendant's land.

[54] Further, the letter from Messrs Dennis Nik & Wong, solicitors for Tan Wei Rong to Messrs Woon Wee Yuen & Partners, solicitors for the first defendant exhibited in TBL-6 said to be the one confirming the final agreed terms was dated 3 December 2014, which is quite some time after the

execution of the tenancy agreement between Tan Wei Rong and China State Construction on 17 September 2014. The said letter also mentioned that the last action on the draft was on 23 October 2014 when it was returned to the first defendant's solicitors, with comments. This is a clear evidence that on a date (23 October 2014) subsequent to the execution of the tenancy agreement (12 September 2014), the draft agreement between the first defendant and Tan Wei Rong had not yet been finalised, let alone agreed. Yet, Tan Wei Rong had in the month prior, already executed the tenancy with China State Construction, which included the sub-letting of the first defendant's land, which he could lawfully only have done after the execution of a tenancy between the first defendant and Tan Wei Rong to confer on the latter the right of the tenancy that he could subsequently sub-let. The execution of that enabling tenancy agreement never took place.

[55] There is no certainty of terms under s. 2 of the Contracts Act 1950 either. Under contract law, the situation in the instant case would fall within the third category of classes referred to in the Court of Appeal decision in *Teh Swee Lip v. Jademall Holdings Sdn Bhd* [2014] 8 CLJ 451 namely that the intention of the parties is not to make a concluded bargain at all, unless and until they execute a formal contract. This is because in the instant case, it is difficult to accept that despite the parties having engaged their own lawyers to help draft the tenancy and subsequently have the drafts reviewed and commented on a number of times, the draft for no good reason then got abandoned and conveniently instead an oral agreement is claimed to have been reached. At the same time, the counterclaim by the second defendant for a declaration on the validity of the tenancy agreement between the first defendant and Tan Wei Rong cannot be sustained, and must therefore be dismissed.

[56] Although the issue is not raised, nor could Tan Wei Rong rely on the *Turquand*'s rule on indoor management and assumed the first defendant had validly authorised him to enter into the tenancy with China State Construction since he would have been aware from his own active involvement in the discussion, as well as through his father, being the second defendant, that the only other director and 50% shareholder of the first defendant (namely, the plaintiff) had not given his consent.

[57] Even though effectively like a *quasi*-partnership, the first defendant is a company incorporated under the Companies Act 1965 and subject to its provisions. I further consider it an exempt private company given its shareholding structure. But the provisions on directors duties apply with equal force to the first defendant company as they do to public listed companies. The second defendant's action and conduct in being supportive of Tan Wei Rong *per se*, being his son are not by themselves necessarily

improper but would be considered to constitute a dereliction in his fiduciary duty for the reasons that first, this tenancy directly involves the interest of the first defendant a company that the second defendant serves as a director. Secondly, Tan Wei Rong is himself conflicted to start with, given his own interest in getting the first defendant's land also rented out to China State Construction, the motivation being that it is adjacent to and provide better access to Tan Wei Rong's own land (the TWR land) which was also rented to China State Construction.

[58] Thirdly, the second defendant had also not cooperated with the plaintiff to have a formal board of directors' meeting or an EGM convened as requested by the plaintiff. Having a formal board meeting or an EGM would have at least restored some semblance of adherence to proper corporate governance on the part at the first defendant company. The second defendant thus did not appear to demonstrate a conduct consistent with that expected of a responsible director and fiduciary of a company when facing the situation, choosing instead for a deadlock and worse still favouring a position that could expose himself to an allegation of breach of duty for conflict of interest.

[59] Therefore, given the absence of a valid tenancy agreement between the first defendant and Tan Wei Rong on the property of the first defendant's land, the latter's entry into the tenancy agreement with China State Construction on that very same property, coupled with at the very least, an acquiesing role played by the second defendant, would in my view represent to the plaintiff a reasonable prospect of the plaintiff's claim on behalf of the first defendant being successful. As stated by the plaintiff, principally, the cause of action would likely be one on the tort of trespass to land. The *Oxford Dictionary of Law* (New Edition) describes trespass to land as follows:

> Trespass to land usually takes the form of entering it without permission. It is no defence to show that the trespass was innocent (eg, that the trespasser honestly believed that the land belonged to him). Trespass to land or goods is a wrong to possession rather than to ownership. Thus a tenant of rented property, for example, has the right to sue for trespass to that property. Trespass to land is a tort but not normally a crime.

[60] Another clear definition is to be found in *Halsbury's Laws of England* (4th edn) vol. 45 at p. 6312 which states:

> Every unlawful entry by one person on land in the possession of another is a trespass for which an action lies, although no actual damage is done. A person trespasses upon land if he wrongfully sets foot on, or rides or drives over it, or takes possession of it, or expels the person in possession, or pulls down or destroys anything permanently fixed to it, or wrongfully takes minerals from it, or places or fixes anything on it or, it seems, if he erects or suffers to continue on his own land anything which invades the

A airspace of another, or if he discharges water from another's land, or sends filth or any injurious substance which has been collected by him on his own land on to another's land.

[61] Accordingly, on the facts and evidence as I have stated, the plaintiff can be said to honestly believe that a good cause of action exists with a B reasonable prospect of success and that his pursuit of the matter is not driven by any collateral purpose as would amount to an abuse of process. Hence, good faith under s. 181B(4)(a) is established.

Question 3: Is It Prima Facie In The Best Interest Of The Company As Per S. 181B(4)(b) For Leave Be Granted?

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[62] Even though the plaintiff may have established good faith, and that a good cause of action with reasonable prospect of success exists, it does not automatically follow that the pursuit of such an action by the first defendant company is necessarily in the best interest of the company. Whilst the Singapore Court of Appeal in *Ang Thiam Swee* preferred to assess the legal D merits or the strength and prospects of the proposed cause of action when considering the question of whether the action is "in the interest of the company" instead of when evaluating whether the complainant is "acting in good faith", the Court of Appeal in *Celcom* followed the test stated in the earlier Singapore case of *Pang Yong Hock & Anor v. PKS Contracts Services* E *Pte Ltd* [2004] SGCA 18 which held that a company may have genuine commercial considerations for not pursuing certain claims, even if those claims may be meritorious.

[63] The second defendant had stated that it had taken the first defendant a very long time to have been able now to finally rent out its land despite F having acquired the same way back in 1995. Nor did the plaintiff show that the rental agreed with China State Construction is below market or even state what the market rental for the first defendant's land should be. Whilst this may be true, the plaintiff was also questioning why the monthly payment to the middlemen is higher than the rental for the first defendant's land.

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[64] In my view, the passage from the Canadian case of *Ontario Ltd v. Bernstein* [2000] OTC Lexis 3480, attributed to *United Copper Securities So Et Al v. Amalgamated Copper Co Et Al* [1917] 244 US 261 cited by the Court of Appeal in *Celcom* would apply to the instant case:

H Whether or not a corporation shall seek to enforce in the courts a course of action for damages is, like other business questions, ordinarily a matter of internal management and is left to the discretion of the directors, in the absence of instruction by vote of the stockholders. Courts interfere seldom to control such discretion *intra vires* the corporation, except where the directors are guilty of misconduct equivalent to a breach of trust, or I **where they stand in a dual relation which prevents an unprejudiced exercise of judgment.** (emphasis added).

[65] Thus in the instant case, the usual disinclination of the courts to interfere in the exercise of a company's commercial discretion and business judgment (as in *Celcom*) would in my view become secondary when there are credible allegations of misconduct or conflict situations. Nor did the second defendant suggest the presence of any basis which could militate against the first defendant pursuing the action such that it would not be in the best interest of the first defendant to do so, other than the contention about the loss of rental from China State Construction. Again, whilst this may be commercially valid an argument, it cannot override the need for the first company to address the wrong perpetuated on the company. Taking into account the position of the second defendant in this case, it can certainly be said that as a director he stands in "a dual relation which prevents unprejudiced exercise of judgment". I therefore hold that the plaintiff has also shown that instituting the derivative action is *prima facie* in the best interest of the first defendant.

[66] It is also worthy of mention that the legislation of the different countries as I set out earlier actually contain differences in their wordings in the statutory formulation on the provisions referable to the "interest of the company", as follows:

(i) Malaysia - "appears *prima facie* to be in the best interest"

(ii) Singapore - "appears to be *prima facie* in the interest"

(iii) Australia - "it is in the best interest"

(iv) Canada - "appears to be in the interest"

Whilst these non-identical formulations were not discussed in *Celcom*, the most stringent seems to be the Australian provision, given the definitive "it is" instead of "appears" and "*prima facie*", as well as use of "best" interest instead of merely "interest". The Court of Appeal's reference to the Canadian and Singapore's precedents in its evaluation of whether the statutory derivative action was in the interest of the company is in my view therefore an accurate representation of the legal position on the point, for being well in accord with the governing Malaysian provision.

Other Key Related Aspects In The Scope Of The Statutory Derivative Action

[67] In evaluating the test of good faith and on whether the action would *prima facie* be in the best interest of the company based either on the *Celcom* or *Ang Thiam Swee* approach, both of which in my view would produce substantially the same results, I have considered four other points of law relevant to statutory derivative actions, none of which was however raised

by the parties in this application. As these aspects are integral to the true scope of the law on statutory derivative action in this country, I am of the view that it is imperative that I should attempt to provide a clear statement of law on the matter.

(1) Must A Plaintiff Be A Minority Shareholder In A S. 181A Action?

[68] The first aspect concerns the status of the plaintiff or person for whom relief under s. 181A is sought. Although common law derivative actions are generally understood to be utilised by minority shareholders, this is not necessarily a pre-requisite to the commencement of derivative actions under s. 181A. In the case of *Dato' Suhaimi Ibrahim & Ors v. Hi-Summit Construction Sdn Bhd & Anor; Konsortium Lapangan Terjaya Sdn Bhd & Ors (Interveners)* [2013] 1 LNS 203, the High Court refused leave under s. 181A (1) on account of the plaintiffs controlling the board of directors and thus they were not considered as "genuinely aggrieved minority", given that the statutory derivative action is to protect the interest of the minority against the wrongdoers who are in control of the board. Although this may be correct, it should be noted that s. 181A does not provide any such criterion as the test to be applied. The Singapore case of *Hengwell Development Pte Ltd v. Thing Chiang Chin* [2002] 4 SLR 902 is authority for the proposition that it can be utilised even by majority shareholders.

[69] There are occasions where majority shareholding may not necessarily be accompanied by the entitlement to the exercise of control. First, the issue of control may be relevant at board level or the general meeting level. It is well entrenched under the Companies Act 1965 that the board is responsible for the management of the business of affairs of the company under s. 131B(1), except where actions by the shareholders in a general meeting are required under the Act. Therefore, if the matter complained of is within the authority of the directors to decide on, which commonly is the case, given that most are management-related decisions such as on the institution and defence of legal suits, a majority shareholder who somehow does not have control at board level (potentially at board of listed entities where the number of independent directors is sizeable or where regulations prohibit the shareholder-appointed directors from voting on account of being "interested") may also be considered as being aggrieved. Even though the power to remove directors in public company is itself vested in the shareholders at a general meeting under s. 128, the corresponding right to appoint new directors may be affected by regulations in certain industry sectors which could prevent the shareholder from having majority control on the board as well.

[70] Secondly, court processes such as injunctions could also thwart an effective exercise of the shareholding rights of the complainant in general meetings despite having majority ownership. In the instant case, despite the

plaintiff's 50% shareholding, the shareholding structure and composition of the board of the first defendant is such that the other shareholder-director could easily by pure inaction, engineer a deadlock as it had effectively happened in this case to paralyse the decision making process of the company at both levels of the board and the general meeting. A Singapore case law authority where leave under s. 216A was granted to address a "deadlock" situation is *Wong Kai Wah v. Wong Kai Yuan & Anor* [2014] SGHC 147 where the defendant, being the only other director (like in the instant case) other than the plaintiff refused to sign the audited accounts of the company

[71] Accordingly, in my view, ultimately, the question to be asked is whether, based on the facts of each particular case, the complainant, being a shareholder (with either a minority or a majority ownership) is able to get the company to take action to seek redress for the wrong done to the company, as perpetuated or facilitated by an insider in a position of influence or control. Therefore, it is strictly not necessary for a plaintiff to be a minority shareholder in order to institute s. 181A of the Companies Act 1965.

(2) Must The Insider Wrongdoer Benefit From The Default In A S. 181A Action?

[72] The second aspect concerns the defendants in an intended derivative action. Derivative actions traditionally and commonly involve suits against the wrongdoers in control such as the miscreant directors who benefited from the wrongdoings. In the English case of *Pavlides v. Jensen* [1956] Ch 565, the shareholder was not successful in his application to commence action on behalf of the company as it was found that the wrongdoing involved a breach of duty of care without the director in default benefiting from the same. Section 181A is silent whether the statutory derivative action can now be expanded to include suits against directors who are only alleged to have been negligent in the discharge of their duties, but do not actually benefit from the breach, a clear departure from "fraud on the minority" situation. By not specifically addressing this point, the Court of Appeal in *Celcom* therefore seems to suggest that this is now the position in Malaysia since no allegation of directors having benefited from the alleged breach was made, although leave was refused for different reasons. There was no allegation of directors benefitting from their alleged wrongdoing in LTAT either. Therefore it should be a correct statement of law that even without the allegation of the defaulting director benefiting from the breach, a mere breach of duty of care by the director that causes loss to the company is also similarly and sufficiently actionable under s. 181A. This is certainly correct both in principle and policy as well, since it further develops the law on derivative action and promotes empowerment of minority rights by indirectly compelling stricter observance by directors of the duties imposed on them, by not confining the type of failures that could justify the granting of leave to commence action. It is therefore not necessarily the case that an action under s. 181A can only be taken if the insider benefits from the wrong done to the company.

A *(3) Must The Insider Wrongdoer Be Sued In A S. 181A Action?*

[73] The third aspect is this. In the instant case, the plaintiff is not seeking to sue the second defendant in the intended derivative action. The plaintiff proposed for the first defendant company to take action against Tan Wei Rong and China State Construction. In the usual case, it would however be B expected that action would be against a breach or wrongdoing by a director, such as the second defendant for having allowed the trespass to the first defendant's land and thereby causing loss to the company as a result, and could even be argued to have possibly benefited given the involvement of his son. However, ss. 181A and 181B do not stipulate the parties against whom C the derivative action may be instituted.

[74] The crux of a derivative action is to allow a complainant to seek leave for the company to institute a suit for a cause of action which has a reasonable prospect of success which otherwise cannot be pursued due to the involvement of a wrongdoer insider having the ability to prevent the filing of the suit by D the company. In my judgment there is no legal necessity for the wrongdoer controller himself to be named as a defendant in a derivative action before leave under s. 181A may be granted, for as long as the suit seeks to enforce the rights of the company which have been violated, against those identified (in addition to the miscreant controller or director) as also being responsible E for the wrongdoing. This proposition in my view is not only sensible for being practical but also well in accord with the mischief against which the derivative mechanism seeks to address, which is to overcome the impediment against proceedings being instituted by the company to enforce its rights against those who have inflicted wrong on the company. The F neutralisation of the obstacle by virtue of the s. 181A derivative action does not necessarily mean that the insider wrongdoer must be sued as it is for the company to decide on its best litigation strategy, for as long as action is against parties whose role or involvement in the wrong perpetrated against it is anything but exculpatory. The overriding focus of s. 181A should be on G pursuing a derivative action against those who have wronged the company, who often are also but not necessarily the insiders who are preventing action from being taken in the first place. But instances where third parties may be involved and participated in the wrongdoing in collusion with insiders cannot be discounted. Whilst it is a pre-requisite for s. 181A derivative action that the insider or controlling element prevents the company from H enforcing its rights (for otherwise action may be brought by the company itself), once the prevention is overcome, it is not the focus of the derivative action to sue those who placed the obstacle, but more to act against the parties who commit the wrong against the company which results in the loss. Whilst the two situations may involve the same parties, they need not

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necessarily be so in all cases. As such, in my view it is not a legal requirement under s. 181A derivative action that the insider in default must be a party to be sued by the plaintiff on behalf of the company.

Can S. 181A Action Be Against Third-party Wrongdoer?

[75] This leads to the final novel aspect (and related to the immediately preceding point) concerning s. 181A relevant to this judgment - which is whether s. 181A, given its history in common law derivative action, can be invoked to permit a plaintiff, on behalf of the company in a derivative action, to commence action against a third party against whom the company may have a cause of action related to the alleged wrongdoing.

[76] It is noteworthy as it is elementary that the common law derivative action is one that is often associated with the need to address a wrong done to the company by a controlling element. Thus, if the company is not prevented from suing a wrongdoer, any cause of action that a company may have against a third party is neither appropriate nor suited to be pursued by way of a derivative action. Although the statute itself is silent on this point, interpretation on its applicability and scope should be formulated towards achieving the objectives of the legislative change. It is clear, from the Report on Corporate Governance by the Finance Committee on Corporate Governance (February 1999) which proposals, coupled with that of the Corporate Law Reform Committee's Consultative Paper on Members Rights and Remedies (2007) triggered the amendments to the Companies Act 1965 (by way of the Companies (Amendment) Act 2007), including the introduction of ss. 181A to 181E, that the overriding objective has always been to further improve the standard of corporate governance in Malaysia. As the earlier part of this judgment has shown, as a relatively recent legislative invention, the scheme of statutory derivative action embodied in ss. 181A to 181E surely can and should at least in legal theory free shareholders seeking redress from the shackles of common law limitations, and that properly reasoned development of new principles of law should be encouraged as it further promotes enrichment of the *corpus juris* of the nation.

[77] In any event, based on my research, such action against third parties can be legally justified in principle if the cause of action against the third party arises from a breach by an insider or controlling element. There is English case law authority which establishes the principle that although the UK legislative provision on derivative action is not expressly limited to proceedings against wrongdoers who are insiders such as directors, leave can only be granted to commence action on behalf of the company against third party wrongdoer if the cause of action against the third party arises from the relevant breach by the directors. Section 261(3) of the UK Companies Act 2006 states the following:

A derivative claim under this Chapter may be brought only in respect of a cause of action arising from an actual or proposed act or omission involving negligence, default, breach of duty or breach of trust by a director of the company. The cause of action may be against the director or another person (or both).

[78] In *Iesini & Others v. Westrip Holdings Ltd & Others* [2009] EWHC 2526 (Ch) Lewison J, in making a noteworthy statement that the new statutory provision has replaced the common law derivative action also made the following observation, which full import in my view is of considerable relevance to our ss. 181A and 181B:

A derivative claim, as defined by Section 260 (3) is not, however, confined to a claim against the insiders. As the concluding part of that sub-section says, the cause of action may be against the director or another person (or both). Nevertheless the cause of action must arise from an actual or proposed act or omission involving negligence, default, breach of duty or breach of trust by a director of the company. A derivative claim may "only" be brought under Part 11 Chapter 1 in respect of a cause of action having this characteristic (although this restriction does not appear to apply to a derivative claim brought in pursuance of an order made under Section 994). Thus the section contemplates that a cause of action may arise from, say, the default of a director, but nevertheless is a cause of action against a third party. A claim against a person who had dishonestly assisted in a breach of fiduciary duty or who had knowingly received trust property would be paradigm examples. It is also to be noted that it is not a requirement that the delinquent director should have profited or benefited from his misconduct. He may be guilty of no more than negligence in managing the company's affairs. However, since the cause of action must arise from his default (etc) a derivative claim brought under Part 11 Chapter 1 will not allow a shareholder to pursue the company's claim against a third party where that claim depends on a cause of action that has arisen independently from the director's default (etc). This view would be consistent with what the Law Commission said in their report Shareholders' Remedies which paved the way for this part of the Companies Act 2006. They said -

> 6.31 So far as the second situation is concerned, one respondent gave the following example. A profitable company is a victim of a tort by a third party and the board, although otherwise committed to the well-being of the company, have ulterior motives of their own for not wishing to enforce the remedy for the tort. Although the board would in those circumstances be in breach of duty, their breach would not have given rise to the claim.
>
> 6.32 We accept that in this type of situation an individual shareholder would have no right to bring a derivative action against the third party tortfeasor under our proposals. (There would of course be potential claim for damages against the directors themselves, although this may give rise to difficulties on causation or quantification, and

it is possible that the directors may not have sufficient funds to meet the claim). However, we do not consider that this is an issue which needs to be addressed for two main reasons.

6.33 First, we are not aware of any cases under the current law where a derivative action has been successfully brought in circumstances such as those described in paragraph 6.31.

6.34 Secondly, (and more importantly) it is consistent with the proper plaintiff principle which we endorsed in the consultation paper and which received virtually unanimous support on consultation. The decision on whether to sue a third party (ie someone who is not a director and where the claim is not closely connected with a breach of duty by a director) is clearly one for the board. If the directors breach their duty in deciding not to pursue the claim then (subject to the leave of the court) a derivative claim can be brought against them. To allow shareholders to have involvement in whether claims should be brought against third parties in our view goes too far in encouraging excessive shareholder interference with management decisions. This is particularly important as we are proposing that derivative actions are to be available in respect of breaches of directors' duties of skill and care. A line has to be drawn somewhere and we consider that this is both a logical and clearly identifiable place in which to draw the line.

[79] Although, unlike the relevant UK provisions, the Malaysian statutory requirements in s. 181A are silent on the grounds for which and against whom, derivative actions can be authorised, I am of the view that the English position, to the extent of the principle that the derivative suit can be pursued against a third party if the claim depends on a cause of action which arises from the director's default, should represent the jurisprudence on statutory derivative action in this country. *lesini* also makes it clear that action may be brought against a director or another person or both, supporting the third preposition as referred to above that it is not a necessity that an insider must be sued as a defendant in an s. 181A suit.

[80] The underlying philosophy should thus be that since derivative actions are for situations where the controller wrongdoer prevents actions from being taken, derivative actions would not be appropriate where first, there are no such constraints, and secondly where the company decides not to pursue against a third party wrongdoer if such decision is not in any way influenced by the third party. In other words, there ought to be some form of collusion or acting in concert between the insider wrongdoer and the said third party to invoke a s. 181A action against the latter. Accordingly, in my view, a derivative action under s. 181A may be instituted even against a third party wrongdoer if the wrong arises from the default of an insider.

[81] In the instant case, the trespass by Tan Wei Rong and China State Construction could be said to have been made possible by the breach of fiduciary duty (or at least of a duty of care) on the part of the second defendant, a director of the company. As such, in addition to the fulfilment of the requirements for leave under ss. 181A and 181B, considering the four propositions of law as I have described above, I held that the derivative action by the plaintiff (who is technically not a minority shareholder), on behalf of the first defendant company, may be commenced against Tan Wei Rong and China State Construction, both being third parties who allegedly committed trespass against the first defendant company given the offending role of the insider second defendant who had preferred taking an acquiescing stance in the face of the trespass but who is himself not being sued.

Conclusion

[82] Accordingly, in conclusion, based on the foregoing reasons, I held that the plaintiff be granted lease under s. 181A as he has on a balance of probabilities satisfied the requirements of s. 181B(4) to justify the same, to commence an action on behalf of the first defendant company against Tan Wei Rong and China State Construction.

[83] The second defendant's counterclaim for a declaration that there is a valid tenancy agreement between the first defendant and Tan Wei Rong in respect of the first defendant's land, and the consequential orders to the execute of the same, is dismissed. Costs of RM1,000 was also awarded to the plaintiff.